

CITY OF SCOTTSDALE

MONTHLY FINANCIAL UPDATE

SEPTEMBER 2006 (JULY/AUGUST 2006 RESULTS)

GENERAL FUND ESTIMATED YEAR-END BALANCE**FY 2006/07 Estimated Fiscal Year-End General Fund Balance**

The following table compares the adopted FY 2006/07 budget plan to the current General Fund balance forecast, incorporating the latest economic estimates and impacts of economic contingency plans.

Estimated Fiscal Year-End 2007 General Fund Balance (In Millions)	FY 2006/07 Budget	FY 2006/07 Current Forecast	Variance Surplus/ (Deficit)	Notes
Beginning Balance July 1, 2006	\$ 64.9	\$ 64.6	\$ (0.3)	(1)
Liabilities Reserve	5.0	5.0	-	
Revenue	246.2	254.9	8.7	(2)
Transfers in	18.7	18.7	-	
Expenditures -- Direct Service	229.9	230.3	(0.4)	(3)
Expenditures -- Debt Service and Other	6.0	6.0	-	
Transfers from General Fund	56.5	57.8	(1.3)	(4)
Estimated Ending Balance June 30, 2007:				
Liabilities Reserve	5.0	5.0	-	
Operating Contingency	6.7	6.3	(0.4)	(5)
General Fund Reserve	30.5	26.6	(3.9)	(6)
Unreserved Fund Balance	0.2	11.2	11.0	(2), (6)
Estimated Total FYE General Fund Balance	\$ 42.4	\$ 49.1	\$ 6.7	

Notes:

1. Beginning Fund Balance has been adjusted for yearend close/audit and includes: 10% Reserve per adopted financial policy, operating budget contingency, reserve for liabilities (i.e., accounts payable and accrued payroll payable from current year resources) and residual unreserved General Fund balance.
2. Primary reason for positive revenue variance is due to State-shared estimates provided by ADOR subsequent to budget adoption. These latest estimates include impacts from mid-decade census and better than expected statewide revenues. Refer to "General Fund Revenue" section for variance analysis and current fiscal year forecast.
3. Includes General Fund operating budget contingency transfer approved by Council on July 10, 2006 for Community Services department expenditures related to youth sports field maintenance. Refer to "Budget Update" section for further discussion on contingency use.
4. Includes projected MPC excise debt service payment related to WestWorld land purchase.
5. See 'Budget Update' section for discussion of contingency use. As of September 12, the City Council has approved the use of \$386,000 of cash from the General Fund operating budget contingency for school sports field maintenance.
6. General Fund Reserve balance is in accordance with City's financial policies adopted by Council. The adopted FY 2006/07 General Fund Reserve balance included funds set aside for potential adverse impacts to the General Fund related to two companies requesting significant tax refund amounts. Subsequently, these two pending issues have been resolved and funds are now reported as part of 'Unreserved Fund Balance'.

GENERAL FUND REVENUE

The following table summarizes key revenues (revenues that change with the economy) that affect the City's General Fund. The table compares the current estimate to the budget plan. Adjustments to the FY 2006/07 current estimates are reflected in the table, along with justifications noted below. The net impact of these adjustments to the revenue bottom line is \$8.7 million over the FY 2006/07 budget plan, primarily reflecting the latest Arizona Department of Revenue state shared revenue estimates provided subsequent to budget adoption, based on the mid-decade census impacts and better than expected statewide revenues.

General Fund Revenues (In Millions)	FY 2006/07 Budget Plan	FY 2006/07 Current Estimate	Variance Surplus/ (Deficit)
Sales Tax ⁽¹⁾	\$ 121.3	\$ 121.3	\$ -
Transient Occupancy (Bed) Tax ⁽¹⁾	1.9	1.9	-
Auto Lieu Tax	9.6	10.0	0.4
Development Permits & Fees	17.0	17.0	-
State Shared Sales Tax ⁽²⁾	20.6	22.4	1.8
State Shared Income Tax ⁽²⁾	20.8	26.6	5.8
Interest Earnings	2.3	3.0	0.7
Other	52.7	52.7	-
Total	\$ 246.2	\$ 254.9	\$ 8.7

Notes:

1. *Sales Tax and Transient Occupancy Tax collections lag by one month (July activity reported in August results).*
 2. *State-shared revenues reflect latest ADOR estimates provided subsequent to budget adoption. These latest estimates include impacts from mid-decade census and better than expected statewide revenues.*
- City Sales Tax collections are **down 0.8** percent fiscal year-to-date over the prior-year period. Category fiscal year-to-date changes over prior year: automotive -8.7 percent, construction -21.2 percent, food stores -3.6 percent, hotels and motels +15.5 percent, major department stores +26.2 percent, miscellaneous retail +2.6 percent, rental +7.7 percent, restaurants +7.6 percent, and utilities +0.5 percent. Adjustments to projected revenues may be made as the year progresses and as important retail periods are reported, such as back-to-school and holiday shopping seasons.
 - Hotel/Motel Transient Occupancy Tax (bed tax) revenue is up 15.5 percent fiscal year-to-date over the prior-year period. The tourism industry continues to experience growth in occupancy and room rates relative to the sub-par performance of the early 2000s. Tourism officials have indicated that industry performance is nearing pre-9/11 levels. However, current economic pressures from high fuel costs and a slowing housing market could negatively affect consumer spending and travel activity.
 - Development Permit and Fee revenue is **down 22.8** percent fiscal year-to-date over the prior-year period. Staff will closely monitor developing revenue trends as the year progresses and make adjustments to revenue projections, if necessary. Development permit and fee revenue is expected to decrease over the next ten years, as the city approaches build out and development shifts from new construction to reinvestment/revitalization.
 - State-Shared Sales Tax receipts are up 65.3 percent year-to-date over the prior-year period. As with the national and local economies, the State is experiencing a relatively strong performance in most sectors of its economy, including sales tax collection. Subsequent to the FY 2006/07 budget adoption, the City received updated state shared revenue figures from the State, which included an increase of \$1.8 million in shared sales tax revenues over the City's adopted FY 2006/07 budget. The increase in shared revenues is attributable to a better than expected pool of revenues statewide, as well as impacts of the mid-decade census data. State-shared revenue receipts will continue to be monitored from the latest Arizona Department of Revenue estimates.

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- State-Shared Income Tax receipts are up 25.65 percent year-to-date over the prior-year period. State Income Tax receipts are received based upon revenue earned by taxpayers **two-years prior**. Subsequent to the FY 2006/07 budget adoption, the City received updated state shared revenue figures from the State, which reflected an increase of \$5.8 million in shared income tax receipts over the City's adopted FY 2006/07 budget. The increase in shared revenues is attributable to a better than expected pool of revenues statewide, as well as impacts of the mid-decade census data. State-shared revenue receipts will continue to be monitored from the latest Arizona Department of Revenue estimates.

GENERAL FUND EXPENDITURES

Estimated Department Expenditure Savings:

Throughout the budget year, this space will be reserved for reporting actual and projected departmental budget savings. As the fiscal year progresses and department expenditure levels and trends develop, staff will be better able to assess and project year-end expenditure savings.

- \$0.8 Million Public Safety Retirement Savings. In late June 2006, the State of Arizona reduced the employer's FY 2006/07 public safety retirement contribution rate by 2.74 percent (from 15.24 percent to 12.50 percent). This rate reduction will save the City approximately \$0.8 million in General Fund retirement costs for sworn police personnel.

BUDGET UPDATE

Revenue Update:

Subsequent to the FY 2006/07 budget adoption, the City received two updates from the State that will favorably impact the General Fund budget by approximately \$8.4 million. First, the City will receive approximately \$7.6 million more in state shared revenue (sales tax \$1.8 million and income tax \$5.8 million) than reflected in the adopted FY 2006/07 budget. The increase in shared revenues is attributable to a better than expected pool of revenues statewide. Second, in late June, the State reduced the employer's FY 2006/07 public safety retirement contribution rate by 2.74 percent (from 15.24 percent to 12.50 percent). This rate reduction will save the City approximately \$0.8 million in General Fund retirement costs for sworn police personnel.

The Highway User Revenue Fund also is expected to see an increase in revenues of more than \$0.6 million over the FY 2006/07 budget due to a projected increase in statewide gas tax revenues.

Staff will continue to monitor the City's FY 2006/07 revenue collections and expenditures on a monthly basis. Revenue forecasting and trend analysis are the foundation upon which the City's FY 2007/08 budget and five-year financial plan are developed.

Budget Process Update:

Financial Services staff is in the process of developing the FY 2006/07 program operating and capital budget planning guides, which will include detailed budget calendars, budget preparation forms, and instructions to the departments for developing their budgets. Staff will continue to explore ways to enhance City Council and citizen input during the FY 2007/08 budget development process. Key dates for this year's budget development cycle are as follows:

- Week of October 2 Capital budget kick-off meeting with City staff
- Week of October 16 Program operating budget kick-off meeting with City staff
- June 5, 2007 Final budget adoption

Contingency Budget Update:

- General Fund Operating Contingency. Throughout the budget year, staff will monitor the \$6.7 million General Fund operating budget contingency for FY 2006/07. As of September 12, the City Council has approved the use of \$386,000 of cash from the General Fund operating budget contingency for school sports field maintenance. The current balance of the General Fund Operating Budget Contingency is approximately \$6.3 million.

On September 19, Council will consider a \$150,000 operating budget contingency transfer to the Community Services Department budget for the operating costs associated with the proposed acquisition and rehabilitation of the former Villa Monterey golf course to an open space park. Also on September 19, Council will consider a \$2.0 million transfer from the General Fund operating budget contingency to the

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CIP for the capital costs associated with the proposed property acquisition and rehabilitation of Villa Monterey.

- CIP Budget Contingency. Staff also monitors the use of the \$4.5 million CIP budget contingency. As of September 12, the City Council has not approved the use of any cash from the CIP budget contingency.

NATIONAL, STATE, AND LOCAL ECONOMIC TRENDS

The table below summarizes some key national and state economic indicators, compares the results to previous actual or forecast, and provides a positive, negative, or neutral trend. Unless otherwise indicated, previous and current values represent a month-to-month comparison in the same year.

Economic Indicators	Month or Quarter	Previous Value	Current Value	Overall Trend***	2007 Estimate
<u>National</u> – Leading Economic Index	July	138.2	138.1	Negative	-
Consumer Confidence	August	107.0	99.6	Negative	-
Consumer Price Index	July	202.9	203.5	Negative	-
Unemployment Rate	August	4.8%	4.7%	Neutral	-
<u>State</u> - Leading Economic Index	May	120.3	120.2	Neutral	-
Arizona Business Conditions Index	August	54.4	60.5	Neutral	-
Arizona Tourism Barometer	May	101.6	103.8	Positive	-
Retail Sales Growth	Forecast*	8.0%	8.1%	Positive	6.8%
Personal Income Growth	Forecast*	8.4%	8.4%	Positive	7.4%
Wage and Salary Employment Growth	Forecast*	4.6%	4.6%	Positive	3.7%
Manufacturing Employment Growth	Forecast*	2.3%	2.3%	Neutral	1.6%
Unemployment Rate	Forecast*	4.3%	4.3%	Neutral	4.4%
Population Growth	Forecast*	3.1%	3.1%	Neutral	2.9%
Hotel/Motel Room Rate (Scottsdale)	July**	\$86.38	\$97.63	Positive	-
Hotel/Motel Occupancy Rate (Scottsdale)	July**	55.6%	53.4%	Neutral	-

*Reflects Arizona Blue Chip Consensus Economic Forecast annual percent change 2006 from 2005 and 2007 from 2006, as of August 2006.

**Reflects over-the-year comparison.

***Overall Trend considers performance of indicators over a three-to-six-month period, not necessarily a month-to-month comparison.

National:

- Leading Index Continues Decline. The U.S. leading index decreased 0.1 percent to 138.1 in July. From January to July, the leading index has fallen by 0.7 percent (a -1.4 percent annual rate), but is still 0.9 percent above its July 2005 level. The leading index has decreased in four of the last six months and the leading index has fallen below its most recent high reached in January. Declining housing permits continued to be the largest negative contributor over this period. The behavior of the leading index the first half of 2006 suggests slow to moderate economic growth should continue in the second half of the year. At the same time, real GDP grew at a 2.5 percent annual rate in the second quarter, following a 5.6 percent gain in the first quarter.
- Consumer Pessimism. Consumer confidence lost significant ground in August and is now at its lowest level this year. The Consumer Confidence Index, which had increased moderately in July, posted a sharp decline in August. The Index is now at 99.6 (1985=100), down from 107.0 in July. Less favorable business conditions and employment outlook resulted in the largest one month decline in confidence since Hurricane Katrina last year. Looking to the future, consumers are growing increasingly more pessimistic about the

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economy's short-term outlook, as consumers' outlook for the next six months turned more negative in August. The outlook for the labor market was also less favorable. The Consumer Confidence Survey is based on a representative sample of 5,000 U.S. households.

- The Consumer Price Index for All Urban Consumers (CPI-U) increased 0.3 percent in July, before seasonal adjustment. The July level of 203.5 (1982-84=100) was 4.1 percent higher than in July 2005.
- Unemployment Steady. Total nonfarm payroll employment increased by 128,000 in August, and the unemployment rate was little changed at 4.7 percent. Payroll employment grew notably over the month in education and health services, while several other industries had modest increases. Average hourly earnings rose by 2 cents, or 0.1 percent, in August following larger gains in the prior 2 months. The number of unemployed persons was at 7.1 million in August. A year earlier, the number of unemployed persons was 7.4 million, and the jobless rate was 4.9 percent.
- Economic Growth Slows during Second Quarter. The nation's Gross Domestic Product grew at a 2.9 percent annual rate in the spring, which was a sharp decline from the first quarter's 5.6 percent pace. The first quarter jump had been the strongest growth spurt in two and a half years. The combination of gasoline prices topping \$3 a gallon and the Federal Reserve raising interest rates during the April-to-June quarter put a tight squeeze on consumer spending, which accounts for two-thirds of the nation's overall economic growth. Inflation moved higher during the spring quarter, as core prices (excluding food and energy) advanced at a rate of 2.8 percent, up from 2.1 percent in the first quarter. The second quarter's increase matched that seen in the first quarter of 2001 and has not been higher since the third quarter of 1994 when this inflation measure rose at a 3.2 percent pace. Consumer spending increased at a rate of 2.6 percent, a tad better than estimated for the second quarter, but a steep deceleration from the first quarter's 4.8 percent.
- Economy Slowing but should Avoid Recession. Job growth has slowed this year, but analysts believe the job market should remain stable in the coming months, which should reduce fears of a recessions. The unemployment rate is expected to stay around the current 4.7 percent rate and new job growth should average 128,000 a month for the remainder of 2006. Gasoline prices are believed to have peaked this year, as prices have come down \$0.19 per gallon in the past three weeks. Labor Day marked the end of the summer driving season, meaning that greater supplies in the coming months should help to keep prices down. Analysts warn, however, that this forecast is based on a benign environment with no serious supply interruptions.
- Back-to-School Sales Boost August Figures. Several retailers achieved passing grades in August, a critical month in the back-to-school shopping season. According to Thomson Financial, of the 40 retailers that have reported same-store results so far, 21 beat estimates, while 19 missed. Same-store sales are measured at stores open at least one year and are a key indication of a retailer's health. August sales are a progress report for the back-to-school retail season, which starts in July and lasts through September. This period is the second most critical time of the year for retailers, behind the Christmas season. Industry experts say the outlook for the rest of the retail year is mixed, as energy costs, interest rates, and a slowing housing market may keep consumers cautious about spending.

Arizona:

- Arizona Business Conditions Index Rebounds. After three months of trending downwards, the Arizona Business Conditions Index began to show improvement in August. The seasonally adjusted Index rose 6.1 points to reach 60.5 in August from 54.4 in July, an 11.2 percent increase. An Index reading of over 50 indicates that the local economy is growing, while a reading below 50 suggests a slowdown in the overall level of economic activity in the near term. Until August, the index had been approaching the critical 50-point mark, below which would indicate a recession. The Arizona Business Conditions Index, which has been published for over 40 years, has accurately predicted every recession with a four- to six-month lead. The Price component of the Index fell by 5.3 percent in August, but still remained at the robust level of 72.7, indicating continued upward pressure on prices. The growth rate of the Price Index increased rapidly in 2003 and has not shown signs of wavering since then.
- Arizona Economy Robust in First Half. According to the consensus forecast from the Arizona Blue Chip panelists, the remainder of 2006 has an overall positive outlook for Arizona, although growth is expected to decelerate as the national economy weakens. Payroll employment is projected to grow by 4.6 percent in 2006, which, if realized, will make this year the second-best year for job growth since 1998. Through the first six months, jobs are up 5.2 percent, only slightly behind last year's 5.3 percent growth pace. Forecasters are calling for retail sales to increase by 8.1 percent in 2006, which will not come close to matching the 13 percent gain in 2005, but still reflects real growth in spending after adjusting for

population growth and inflation. Arizona's residential single-family resales dropped 26.9 percent in the second quarter – the steepest of any state. However, should metro Phoenix resales finish 2006 as much as 40 percent below last year, it will still be the fourth-strongest year for resales in state history. Also, single family permits are down more than 20 percent versus last year, as even slower growth in new home activity is expected in the months ahead. But as with resales, even a 20 percent drop in building permits would still make 2006 the third-strongest year for single-family building in Arizona history.

SCOTTSDALE BUSINESS ACTIVITY (PRESENTED BY ECONOMIC VITALITY)

- **InNexus Biotechnology Inc.**, headquartered in Scottsdale on the campus of Mayo Clinic, announced the appointment of Jeff Morhet as its new CEO and president. InNexus is an innovative antibody-driven drug development company that has developed two technology platforms, SuperAntibody™ and TransMAbs™, which improve the potency of existing antibody products while opening new markets and disease applications.
 - Chicago-based **Strategic Hotels & Resorts Inc.** has agreed to pay \$345 million for the 651 room Fairmont Scottsdale Princess and \$15 million for an abutting 10 acres. The hotel was developed in 1987 on 65 acres. The property averages an above market 79 percent occupancy rate.
 - **Mobility Electronics Inc.**, a leading provider of innovative portable power and computing solutions for the mobile electronic device user, announced that the company is now shipping the iGo power splitter accessory. This new power accessory is designed to work with select iGo adapters to simultaneously charge two mobile electronic gadgets, such as mobile phones, Bluetooth® headsets, smartphones/PDAs, MP3 players, portable gaming devices, and digital cameras, from a single adapter.
 - Hot Stix Mobile, a division of Scottsdale-based **Hot Stix Golf**, signed a contract with three leading golf equipment manufacturers (Titleist, Cobra, and Nike) to carry their clubs on the company's mobile centers that travel to major US golf events and destinations. The centers provide onsite fitting and custom club building services, matching a golfer's unique swing to equipment for maximum results.
 - Congressman J.D. Hayworth (R-AZ) and Department of Commerce Assistant Secretary Al Frink toured **Kyocera Solar, Inc.'s headquarters and integration facility in Scottsdale** in early September to learn about its manufacturing, integration, and integrated solar energy applications development. After touring Kyocera's 52,000 square foot facility, they joined in a roundtable discussion on the emerging solar industry. Kyocera Solar, Inc. is a world-leading supplier of environmentally sound, solar electric energy solutions. It is a wholly owned subsidiary of Kyocera International, Inc. of San Diego, the North American headquarters and holding company for Kyoto, Japan based Kyocera Corporation..
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